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CD corporate disputes

MANAGING PRODUCT LIABILITY & LITIGATION IN THE AUTOMOTIVE SECTOR

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EXPERT FORUM

MANAGING PRODUCT LIABILITY & LITIGATION IN THE AUTOMOTIVE SECTOR

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CD: Reflecting on the last 12-18 months or so, what types of disputes are you seeing arising from product liability in the automotive sector?

Egler: In the consumer and manufacturer relationship, 'Dieselgate' led to an increasing number of lawsuits in Germany due to the threat of statutes of limitations. Unlike US class actions, in many countries of the EU there are no class actions in the strict sense. The lack of an effective collective redress regime also had a huge impact on German courts, many of which were swamped by nearly 50,000 lawsuits brought on by individual customers. This wave of litigation was obviously too much for the court system to handle. In response to this situation, German lawmakers recently introduced collective actions in the form of model declaratory actions to simplify and accelerate court procedures. The approach taken by German lawmakers is generally in line with the collective redress systems in place in many other countries in Continental Europe, such as Italy and Spain. Model declaratory actions provide qualified associations with the ability to file for determination of the existence or non-existence of factual and legal prerequisites in the consumer and manufacturer relationship. Under the new regime, consumers are able to base their individual claims on these prerequisites if they have registered for the individual model declaratory action. Several model declaratory actions are pending at higher courts in connection with Dieselgate. The effects of this new instrument concerning product liability cases are still unknown. However, we believe that these new opportunities for collective redress will also become more important for product liability cases.

Adams: Voluntary automotive recalls continue to serve as a springboard for product liability cases and consumer fraud class actions. While product liability injury case filings continue to decline, the types of cases being filed are larger, more catastrophic-injury cases. With consumer fraud class actions, there has been a general reduction in overall filings in the last 12 to 18 months, though historical cycles have seen lulls followed by waves of new filings. Many recent consumer fraud class actions have featured issues related to new technology, such as performance of crash avoidance technology, alleged hardware and software vulnerabilities and technological obsolescence. Parens patriae cases by state attorneys general or local district attorneys continue, though much less prolifically than the levels seen in recent years. In many instances, these cases are prosecuted by plaintiff law firms contracted to pursue the case for the county or, to a lesser degree, the state. The most sizeable growth has been in individual consumer protection or warranty claims invoking fee-shifting statutes and a 'mass-tort' model. These lawsuits have led some courts

to reassess their treatment of this evolving form of aggregate individual automotive litigation matters, with increasing use of coordinated or centralised proceedings.

Smith: Automotive sector product liability actions predominantly involve classic personal injury claims based on alleged defects. Plaintiffs' attorneys leverage recalls related to motor vehicle safety to support personal injury claims – often in the absence of factual allegations or evidence showing that the defect at issue caused or contributed to a specific accident or injuries. Plaintiffs are also increasingly relying on product liability defect claims as a basis to bring putative economic loss class actions, alleging damages in the form of overpayment or decrease in value as a result of the alleged defects.

"With consumer fraud class actions, there has been a general reduction in overall filings in the last 12 to 18 months, though historical cycles have seen lulls followed by waves of new filings."

Rob Adams,
Shook, Hardy & Bacon LLP

CD: Are there any common factors driving these disputes?

Adams: Fewer but higher-exposure product liability cases are being filed largely because of the ever-increasing costs of preparing these cases, typically without any kind of fee-shifting mechanism. This, in part, explains the migration of many plaintiff product liability lawyers into the class action space or individual consumer protection claim cases, where work-up costs are lower and potential net pay off is higher. The downtick in state attorneys general actions may relate in part to the fact that there have been few highly publicised incidents and litigations in 2018 as compared to the highly public litigations in the preceding five years. The technology-related claims likely arise from the tension between consumer demand for more highly automated and connected features, misaligned expectations and the real-world readiness of such emerging technologies. Distractions while driving have always existed, but they continue to escalate with the continuous release of more interactive and engaging features.

Smith: On an individual basis, a sympathetic plaintiff and serious injury continue to drive many lawsuits. Plaintiffs' attorneys frequently rely on high-profile recalls or voluminous warranty claims

to identify and bring personal injury and defect related economic loss class actions. The increase of social media forums offers an additional avenue for plaintiffs' attorneys to monitor and identify complaints about potential defects. These sources are increasingly cited by plaintiffs' lawyers in support of consumer fraud or economic loss putative class actions. There is a growing trend of bringing these claims even in the absence of a single alleged accident or injury purportedly caused by the defect.

Egler: Generally speaking, pricing pressure and the introduction of new technologies applied by original equipment manufacturers (OEMs) has led to an increasing number of disputes. Based on our experience, the desire of suppliers to defend themselves against the claims of OEMs has risen. OEMs publish and assert more and more favourable terms and conditions on their behalf. On the flipside, these terms and conditions are less favourable to suppliers. For example, supplier contracts by OEMs contain clauses under which suppliers are obliged to reimburse for damages with unknown causes. Under German law, such clauses are often not legally binding or void. Furthermore, we see a steep increase in arbitration proceedings to resolve disputes along the automotive supply chain – especially where suppliers originate from, and have their assets in, Asia and Latin America. Traditionally, German companies active in the automotive sector in particular have preferred 'German courts', but this has apparently changed. One reason might be the problems with enforcing court judgements in many countries outside of Europe and North America.

"The landscape of product liability class actions is shifting and this applies with equal force in the automotive sector."

Renee D. Smith, Kirkland & Ellis LLP

CD: What advice would you offer to automotive companies on dealing with product liability-related class actions? What lessons can they draw from recent cases?

Egler: In Germany, there is no direct equivalent to US class actions. Our experience in high volume product liability cases in the manufacturer and supplier relationship shows that assessing the damage claimed by plaintiffs can be crucial. The

alleged damage often contains discrepancies or positions which are not covered as damages under German law. Regarding the consumer and manufacturer relationship, Dieselgate is exemplary for the challenges of high volume litigation cases in Germany. Taking the newly introduced model declaratory actions into account, the number of disputes between consumers and manufacturers will most likely further increase. Thus, manufacturers will be met with a higher number of individual claims of customers in total, since model declaratory actions allow a higher number of individual customers to file their claims in product liability cases. This leaves the manufacturer exposed to the risks of many individual claims. Therefore, extrajudicial and court settlements as well as manufacturer-sided substitution programmes are highly significant.

Smith: The landscape of product liability class actions is shifting and this applies with equal force in the automotive sector. The practical effects of the landmark US Supreme Court decision in *Bristol-Myers* continue to evolve. Automotive companies should invoke *Bristol-Myers* and its progeny to curtail the practice of joining in one complaint multiple plaintiffs from different states who were involved in different accidents under state joinder rules. Automotive companies have also relied on the *Bristol-Myers* opinion with varying degrees of success to limit sprawling, multi-state class actions brought in 'plaintiff-friendly' jurisdictions. Automotive companies should assess and raise these issues early in the case to avoid waiver.

Adams: Until further tort reform is adopted, automotive companies will remain subject to an unfair risk of exposure from no-injury and low-injury class action claims, as well as abuses of fee-shifting consumer protection and warranty statutes. Critical and creative planning by the engineering, product safety, consumer affairs and legal teams is necessary to prepare a strong defence. This begins during product development and approval and includes preparing risk-mitigation plans that help automotive companies prepare for and respond to any claims, lawsuits or potential regulatory issues that may follow. A reputation of good corporate citizenship bolstered by appropriate and swift communication and response goes a long way, too. Creative pre-suit risk mitigation and avoidance strategies are also critical, such as assessing advertising claims and warnings and assessing the use of contractual arbitration clauses to limit litigation exposure.

CD: What additional challenges do cross-border and multinational disputes tend to bring? What general steps can automotive companies take to manage these obstacles?

Smith: The sale and manufacture of vehicles draw upon multinational sources, both within the

company and in connection with outside suppliers. Vehicle manufacturers face distinct regulatory requirements and standards across borders. It is important that companies recognise and understand these differences, particularly where litigation involves alleged violations regarding vehicle architecture and regulatory schemes that are different from those in the US or elsewhere.

Egler: When negotiating contracts, companies should carefully consider which forum and jurisdiction they agree to. It might be tempting – for a party with bargaining leverage – to force a contractual counterparty to accept the jurisdiction of the courts at their company's headquarters. But one should always check whether a judgement rendered by these courts would actually be enforceable in the country where the counterparty has its assets. Winning a case does not necessarily mean getting your money. Legally, the key issue may be the difference in rules dealing with product liability cases with regard to the later assessment and allocation of liability and damages along the supply chain in different legal systems. Here, issues of the applicable law are most relevant. Careful consideration should be made by suppliers in the supply chain about which jurisdiction should govern the contract. Manufacturers of products sold to consumers, on the other hand, have no choice – the laws of the country in which the consumer lives normally apply. Furthermore, linguistic differences when negotiating and drafting contracts can lead to different interpretations of key clauses. Therefore, legal counsel should be utilised when concluding supply contracts, in order to preclude these issues from a product liability perspective.

Adams: With varying e-discovery and privacy requirements across the world, manufacturers are increasingly challenged to create, preserve and obtain the desired information to respond to inquiries and defend litigation. For example, the transfer of personal information out of the European Union may implicate specific notice and consent requirements under the General Data Protection Regulation (GDPR). In anticipation of product liability issues arising, manufacturers need a proactive policy and strategy that satisfies compliance but affords access to information required in different jurisdictions to effectively address inquiries, claims and lawsuits as they occur. Courts on the whole remain insufficiently deferential to privacy statutes in other countries, oftentimes ordering production without regard to the penalties that could be faced by the foreign corporate affiliate.

CD: Could you outline some of the key issues in relation to autonomous driving, and the impact on the automotive industry of new players like Microsoft, Intel and others? How are these issues

affecting product liability and the approach to risk?

Egler: One of the key issues in relation to autonomous driving in Germany is the uncertainty regarding strict liability of consumers and manufacturers. On the one hand, vehicle owners are subject to strict liability under traffic law. A corresponding liability system for manufacturers is yet to be put in place. In addition, manufacturers are strictly liable under German law for consequential damage resulting from the use or consumption of their products if the damage is caused by a defect in that product. It is uncertain whether autonomous systems are considered as one product or just one part of the whole vehicle product. The result of the latter would mean that damage to the vehicle itself would not be subject to strict liability. The entry of Microsoft as supplier of an automotive cloud and Intel as an automotive supplier, poses different challenges to the automotive industry. Microsoft and Intel, as global players who are not solely reliant on

the automotive sector, will further change the power dynamic in the automotive industry. In the past, the bargaining power clearly rested with the OEMs, which dictated terms and conditions, or at least tried to. This will likely change as more and more potent international tech companies enter the automotive market.

Adams: Identification of a responsible party and the boundaries of those obligations, especially with artificial intelligence (AI), is a growing challenge. When vehicles reach stage three, and driver vigilance is no longer required, there will still be crashes, and fault and financial responsibility will need to be assigned for personal injury claims, vehicle code violations, insurance premium ratings and tort claims if injuries are involved. Traditional product liability infrastructure holds manufacturers responsible, but the interplay between AI, automated vehicles (AV) and highly automated vehicles (HAV) requires greater focus to upfront allocation of risk by technology developers, suppliers and service providers to insulate manufacturers from exposure they cannot control.

Smith: Autonomous driving has ushered in a new wave of liability risks for the automotive industry. In addition to the liabilities associated with designing and manufacturing a vehicle, autonomous driving companies may face liabilities claims traditionally associated with the driver of a vehicle. Further, with new entrants in the automotive field, there is no well-established relationship among these companies regarding product liability-risk allocation. The old and new players should consider carefully delineating roles, responsibilities and assumption of litigation-related risks should they arise. In addition, these new players may have more diverse customer and industry bases than traditional automotive suppliers, which may shift the bargaining power in terms of allocation of risks and responsibilities.

> **"Connected driving gives rise to new data protection issues in connection with the GDPR in Europe. One of the key issues is the necessity to obtain consumer consent."**
>
> *Philipp Egler, Bird & Bird LLP*

CD: Developments in connected driving could give rise to potential for third-party risk with telecoms companies. What are

automotive companies doing to manage this new frontier of liability?

Adams: Vehicles continue to contribute to the information technology landscape. Automotive companies, some striving to be mobility companies, are now also technology and data companies. In this new frontier for automakers, potential liability expands to include claims involving data breaches, insufficient disclosures and privacy-related security concerns. To mitigate these risks, automobile manufacturers are taking a closer look at the data their vehicles are collecting and how that data is being protected and used. Companies are also transferring the risks with cyber liability insurance and indemnification provisions in vendor contracts.

Smith: The interaction among telecom companies and vehicle manufacturers offers more sophisticated partnering opportunities, but also more complex risk relationships. The scope and division of potential liability is largely uncharted and may be clarified in the coming years through regulatory action at the federal, state and local level. It is critical that companies proactively monitor regulatory and related actions in assessing and reducing risks. It is important that automobile companies follow the evolving regulatory and legal landscape, and where appropriate, engage in cooperative and transparent relationships with regulatory agencies.

Egler: Connected driving gives rise to new data protection issues in connection with the GDPR in Europe. One of the key issues is the necessity to obtain consumer consent. Communication between vehicles and traffic infrastructure is a precondition to autonomous driving. Autonomous vehicles therefore constantly exchange location and movement data. High encryption standards are needed to protect customer data. The cooperation of Microsoft and VW shows that automotive companies rely heavily on technology suppliers to develop smart and secure systems. Even more importantly, automotive suppliers will need to find a way to close liability gaps within the supply chain when it comes to cyber-physical systems. Most warranty laws in European countries still reflect the 'old world' and are designed for claims concerning defective hardware. If, however, connectivity to mobile networks becomes an integral part of the product, these old regimes do not adequately address the specific problems. It is essential for automotive suppliers to update their contractual documentation accordingly.

CD: Why is it so important for automotive companies to take a proactive approach to managing risks? What essential advice would you offer on product safety reviews, designed recall processes and triggers, for example?

Egler: Proactively mitigating risks in a timely manner, before they pose a concrete threat to vehicles and the public, is of fundamental importance. Apart from severe liability risks and hence a huge cost risk, the public image of automotive companies and thus public trust might easily be damaged. Manufacturers should educate themselves on the legal requirements in those countries where they sell their products. In most EU countries, manufacturers are obliged to supervise the product safety risks of their products. Therefore, regular safety reviews are extremely important. Designed recall processes and triggers allow the manufacturer to act in an ad hoc manner. With these tools, manufacturers can save face in public and prevent further damage. Therefore, these systems should be regularly reviewed and optimised.

Smith: This is an exciting and innovative time in the automotive industry. Companies have the opportunity to improve upon already-sophisticated product safety review processes. Encouraging employees and others to share any concerns will help companies identify and remedy potential issues earlier, and may avoid the need for a recall or other action later. In addition, transparent sharing of information with regulatory agencies may lead to cooperative relationships and will improve overall safety across the industry. By working with these agencies and regulators, companies will also increase the ability to assess and minimise related regulatory and litigation risks.

Adams: Proactive efforts are critical to mitigate and control risk exposure, especially in the world of AI, where not even the manufacturers are in control of what is coming next. Effectively integrating product safety and legal team input at stage-gate phases in product development, and ensuring regular product safety and legal team evaluation of potential failure modes and effects and real world field performance issues as they arise, will provide for greater awareness and more effective realisation on policies and objectives for continued product safety. Now, more than ever, is the time for proactive, thoughtful input to ensure consumer demands and creative concepts do not outpace technological capabilities. CD